



中国人民财产保险股份有限公司  
PICC Property and Casualty Company Limited



2004

Interim Report

## CORPORATE INFORMATION

Registered name:	Chinese name: 中國人民財產保險股份有限公司 English name: PICC Property and Casualty Company Limited
Main business:	The Company provides a broad range of non-life insurance products in the PRC. The major scope of business include motor vehicle insurance, commercial property insurance, homeowners insurance, cargo insurance, liability insurance, accidental injury insurance, surety insurance and short-term health insurance business denominated in both RMB and foreign currencies, together with related reinsurance business.
Place of listing:	The Stock Exchange of Hong Kong Limited
Type of stock:	H Shares
Name of stock:	PICC P&C
Stock code:	2328
H share registrar:	Computershare Hong Kong Investor Services Limited
Place of business:	No.69 Dongheyan Street, Xuanwumen , Beijing 100052, PRC
Legal representative:	Tang Yunxiang
Secretary of the Board of Directors:	Fu Zhu
Company Secretary:	Man Kam Ching
Information inquiry department:	Secretariat of the Board of Directors
Auditors:	Ernst & Young
Consulting actuaries:	Milliman Asia Limited
Legal advisers:	<i>as to Hong Kong law:</i> Linklaters  <i>as to PRC law:</i> King and Wood

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## CONDENSED PROFIT AND LOSS ACCOUNT

For the six months ended 30 June 2004

	Notes	Unaudited Six months ended 30 June 2004 RMB million	Pro forma Six months ended 30 June 2003 RMB million (Note)
TURNOVER	4	35,389	30,651
Net premiums earned	4	24,206	19,930
Interest and dividend income	4	519	301
Net gains/(losses) on trading and non-trading securities	4	(514)	230
Net claims incurred	5	(17,586)	(14,253)
Amortisation of deferred acquisition costs		(1,626)	(1,029)
Insurance protection expense		(325)	(258)
Interest expense credited to policyholders' deposits		(78)	(58)
General and administrative expenses		(3,240)	(2,929)
OPERATING PROFIT	6	1,356	1,934
Finance costs		(66)	(11)
PROFIT BEFORE TAX		1,290	1,923
Tax	7	(327)	(602)
NET PROFIT ATTRIBUTABLE TO SHAREHOLDERS		963	1,321
BASIC EARNINGS PER SHARE (in RMB)	9	0.086	0.165

Note: The pro forma condensed profit and loss account of the Company for the six months ended 30 June 2003 was extracted from the Accountant's Report as set out in the Company's prospectus dated 27 October 2003.

## CONDENSED BALANCE SHEET

30 June 2004

		Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
	Notes		
<b>ASSETS</b>			
Cash and cash equivalents	10	22,135	18,004
Deposits with banks and other financial institutions	10	9,448	12,562
Trading securities	11	6,061	6,094
Non-trading securities	12	15,126	10,765
Held-to-maturity securities	13	1,100	—
Premiums receivables and agents' balances, net	14	4,090	2,012
Unearned premium reserves — reinsurers' share		5,574	6,030
Receivables from reinsurers	15	878	656
Reinsurance recoverable on unpaid losses		7,070	6,283
Prepayments and other receivables	16	2,437	2,067
Capital security fund		2,228	2,228
Fixed assets		14,980	15,645
Construction in progress		702	642
Deferred acquisition costs		1,644	1,284
Other non-current assets		232	300
<b>TOTAL ASSETS</b>		<b>93,705</b>	<b>84,572</b>
<b>LIABILITIES</b>			
Unearned premium reserves		36,346	30,422
Loss and loss adjustment expense reserves		20,688	17,956
Policyholders' deposits		9,154	9,290
Payables to reinsurers	17	1,713	1,978
Accrued insurance protection fund		835	522
Tax payable		505	167
Other liabilities and accruals		5,150	5,147
Deferred tax liabilities		5	333
<b>TOTAL LIABILITIES</b>		<b>74,396</b>	<b>65,815</b>
<b>CAPITAL RESOURCES</b>			
Issued capital	18	11,142	11,142
Reserves/owners' equity		6,167	5,615
		17,309	16,757
<b>SUBORDINATED LOAN</b>	19	<b>2,000</b>	<b>2,000</b>
<b>TOTAL LIABILITIES AND CAPITAL RESOURCES</b>		<b>93,705</b>	<b>84,572</b>

# STATEMENT OF CHANGES IN EQUITY

For the six months ended 30 June 2004

	Issued share capital RMB million	Share premium account RMB million	Non-trading investment securities revaluation reserve RMB million	Statutory surplus reserve RMB million	Statutory public welfare fund RMB million	Owners' equity / other reserves RMB million	Retained profits RMB million	Total RMB million
<b>Unaudited</b>								
At 1 January 2004	11,142	4,739	(5)	6	3	774	98	16,757
Revaluation of investments in non-trading securities	—	—	(610)	—	—	—	—	(610)
Deferred tax assets recognised	—	—	199	—	—	—	—	199
Net loss not recognised in the profit and loss account	—	—	(411)	—	—	—	—	(411)
Net profit for the period	—	—	—	—	—	—	963	963
At 30 June 2004	11,142	4,739	(416)	6	3	774	1,061	17,309
<b>Pro forma (Note (b))</b>						(Note(a))		
At 1 January 2003	—	—	—	—	—	10,293	—	10,293
Pre-incorporation revaluation of investments in non-trading securities	—	—	—	—	—	85	—	85
Revaluation surplus realised	—	—	—	—	—	(5)	—	(5)
Pre-incorporation recognition of change in deferred tax assets	—	—	—	—	—	(27)	—	(27)
Net gain recognised in the profit and loss account	—	—	—	—	—	53	—	53
Pre-incorporation net profit for the period	—	—	—	—	—	1,321	—	1,321
At 30 June 2003	—	—	—	—	—	11,667	—	11,667

Note (a): This represents the net profit during the period from 1 October 2002 to 6 July 2003 arising from the commercial insurance business injected into the Company, net of the special dividends payable, pursuant to the Reorganisation (see note 1 to interim financial statements). According to a legal opinion obtained from the Company's PRC legal counsel, this amount is distributable, subject to the provisions as set out under "Profit appropriation" in note 3 to the Company's first set of financial statements for the period from 7 July 2003 (date of incorporation) to 31 December 2003.

Note (b): The pro forma statement of changes in equity of the Company for the six months ended 30 June 2003 was extracted from the Accountant's Report as set out in the Company's prospectus dated 27 October 2003.

# CONDENSED CASH FLOW STATEMENT

For the six months ended 30 June 2004

	Unaudited Six months ended 30 June 2004 RMB million	Pro forma Six months ended 30 June 2003 RMB million (Note)
Net cash inflow from operating activities	8,102	7,286
Net cash outflow from investing activities	(3,132)	(2,182)
Net cash inflow/(outflow) from financing activities	(839)	1,064
NET INCREASE IN CASH AND CASH EQUIVALENTS	4,131	6,168
Cash and cash equivalents at beginning of period	18,004	11,629
CASH AND CASH EQUIVALENTS AT END OF PERIOD	22,135	17,797

Note: The pro forma condensed cash flow statement of the Company for the six months ended 30 June 2003 was extracted from the Accountant's Report as set out in the Company's prospectus dated 27 October 2003.

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## 1. BASIS OF PRESENTATION

Pursuant to the reorganisation of the People's Insurance Company of China (the "Reorganisation"), which took effect as of 30 September 2002, the Company was incorporated on 7 July 2003 as a joint stock company with limited liability in the People's Republic of China (the "PRC"). Further details of the Reorganisation are set out in the Company's prospectus dated 27 October 2003 issued in respect of the listing of the Company's shares on the Main Board of The Stock Exchange of Hong Kong Limited ("HKSE").

The Company's unaudited interim financial statements have been prepared in accordance with the requirements of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Main Board Listing Rules"), including compliance with Statement of Standard Accounting Practice 25 "Interim financial reporting" of the Hong Kong Financial Reporting Standards issued by the Hong Kong Society of Accountants. The accounting policies adopted are consistent with those set out in the Company's first set of financial statements for the period from 7 July 2003 (date of incorporation) to 31 December 2003 except for the first adoption of an accounting policy as set out below in relation to held-to-maturity securities due to the purchases of certain dated debt securities during the six months ended 30 June 2004.

The prior period comparative figures included in the interim financial statements are prepared as if the Company had been in existence throughout the six months ended 30 June 2003 and as if the Company's Reorganisation was effective prior to the earliest date presented therein.

The interim financial statements are unaudited, but have been reviewed by the Company's Audit Committee and Ernst & Young, the Company's auditors. Ernst & Young's independent review report to the Board of Directors is set out on page 22.

### Held-to-maturity securities

Held-to-maturity securities are investments in dated debt securities which the Company has the expressed intention and ability to hold to maturity, and are stated at amortised cost less any impairment losses which reflect their credit risk. Amortised cost is cost plus or minus the cumulative amortisation of the difference between the purchase price and the maturity amount. An impairment loss is charged to the investment and profit and loss accounts in the period in which it arises, on an individual investment basis. In situations where the circumstances and events which led to an impairment of a held-to-maturity security cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future, the reversal of the impairment is credited to the profit and loss account, on an individual investment basis, to the extent of the amount previously charged.

## 2. CORPORATE INFORMATION

The registered office of the Company is located at 69 Dongheyan Street, Xuanwumen, Beijing 100052, PRC. The Company is a provider of commercial insurance coverage in the PRC, and provides a wide range of property and casualty (“P&C”) insurance consisting of property loss and damage insurance, liability insurance, credit and guarantee insurance, accidental injury insurance, short term health insurance and other P&C insurance as well as related reinsurance.

In the opinion of the directors, the ultimate holding company is PICC Holding Company, which is incorporated in the PRC.

## 3. SEGMENT INFORMATION

Line of business segments have been presented as the Company’s primary segment reporting basis. No analysis of the Company’s turnover and contribution to profit from operations by geographical segment has been presented as all the Company’s operating activities are carried out in the PRC.

Summary details of the business segments are as follows:

- (a) the motor vehicle segment provides insurance products covering motor vehicles;
- (b) the commercial property segment provides insurance products covering commercial properties;
- (c) the homeowners segment provides insurance products covering homeowners and their homes;
- (d) the cargo segment provides insurance products covering vessels, crafts or conveyances;
- (e) the liability segment provides insurance products covering policyholders’ liability;
- (f) the accidental injury segment provides insurance products covering accidental injury; and
- (g) the “other” segment mainly represents insurance products related to marine hull, aviation and oil and gas.

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## 3. SEGMENT INFORMATION (Continued)

Information on the Company's reportable business segments is as follows:

	Unaudited Six months ended 30 June 2004 RMB million	Pro forma Six months ended 30 June 2003 RMB million
<b>Turnover</b>		
Motor vehicle	24,197	19,387
Commercial property	5,145	5,221
Homeowners	793	736
Cargo	1,527	1,555
Liability	1,094	1,412
Accidental injury	836	849
Other	1,797	1,491
	35,389	30,651
<b>Net premiums earned</b>		
Motor vehicle	16,377	13,028
Commercial property	3,238	3,441
Homeowners	378	604
Cargo	1,710	1,177
Liability	942	1,112
Accidental injury	851	37
Other	710	531
	24,206	19,930
<b>Interest and dividend income</b>		
Homeowners	53	99
<b>Net gains/(losses) on trading and non-trading securities</b>		
Homeowners	(7)	58

## 3. SEGMENT INFORMATION (Continued)

	Unaudited Six months ended 30 June 2004 RMB million	Pro forma Six months ended 30 June 2003 RMB million
<b>Net claims incurred</b>		
Motor vehicle	(14,096)	(10,708)
Commercial property	(1,248)	(1,605)
Homeowners	(103)	(178)
Cargo	(459)	(574)
Liability	(561)	(795)
Accidental injury	(553)	(31)
Other	(566)	(362)
	(17,586)	(14,253)
<b>Amortisation of deferred acquisition costs</b>		
Motor vehicle	(1,328)	(895)
Commercial property	(133)	(60)
Homeowners	(47)	(77)
Cargo	(118)	(61)
Liability	(72)	(41)
Accidental injury	(53)	(3)
Other	125	108
	(1,626)	(1,029)
<b>Insurance protection expense</b>		
Motor vehicle	(231)	(168)
Commercial property	(45)	(42)
Homeowners	(8)	(7)
Cargo	(14)	(13)
Liability	(10)	(12)
Accidental injury	(8)	(7)
Other	(9)	(9)
	(325)	(258)
<b>Interest expense credited to policyholders' deposits</b>		
Homeowners	(78)	(58)
<b>Segment profit/(loss) before unallocated income and expenses</b>		
Motor vehicle	722	1,257
Commercial property	1,812	1,734
Homeowners	188	441
Cargo	1,119	529
Liability	299	264
Accidental injury	237	(4)
Other	260	268
	4,637	4,489

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## 3. SEGMENT INFORMATION (Continued)

	Unaudited Six months ended 30 June 2004 RMB million	Pro forma Six months ended 30 June 2003 RMB million
Unallocated operating income and expenses		
Interest and dividend income	466	202
Net gains/(losses) on trading and non-trading securities	(507)	172
General and administrative expenses	(3,240)	(2,929)
Finance costs	(66)	(11)
	(3,347)	(2,566)
Profit before tax	1,290	1,923
Tax	(327)	(602)
Net profit	963	1,321

Interest and dividend income and net gains/(losses) on trading and non-trading securities attributed to the homeowners insurance product, which can be separately identified based on the results of its designated pool of investments, are separately disclosed. The remaining amounts, which are not attributed to particular insurance products, are not allocated and are included under unallocated operating income and expenses.

#### 4. TURNOVER AND REVENUE

Turnover represents direct premiums written and reinsurance premiums assumed, net of government levies and surcharges.

An analysis of turnover, interest and dividend income and net gains/(losses) on trading and non-trading securities is as follows:

	Unaudited Six months ended 30 June 2004 RMB million	Pro forma Six months ended 30 June 2003 RMB million
<b>Turnover</b>		
Direct premiums written	37,395	32,392
Reinsurance premiums assumed	1	4
	37,396	32,396
Less: Government levies and surcharges	(2,007)	(1,745)
	35,389	30,651
<b>Net premiums earned</b>		
Turnover	35,389	30,651
Less: Reinsurance premiums ceded	(4,803)	(5,720)
	30,586	24,931
Less: Changes in net unearned premium reserves	(6,380)	(5,001)
	24,206	19,930
<b>Interest and dividend income</b>		
Interest income from trading and non-trading securities	176	30
Interest income from deposits with banks and other financial institutions	203	129
Interest income from held-to-maturity securities	3	—
Dividend income from trading and non-trading securities	137	142
	519	301
<b>Net gains/(losses) on trading and non-trading securities</b>		
Realised gains on trading securities — Mutual funds	4	8
Realised gains on trading securities — Debts	3	7
Unrealised gains/(losses) on trading securities — Mutual funds	(471)	170
Unrealised gains/(losses) on trading securities — Debts	(80)	27
Net gains on disposal of non-trading securities:		
Realisation of revaluation reserve previously recognised	1	5
Recognised gain arising in the period	29	13
	(514)	230

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## 5. NET CLAIMS INCURRED

	Unaudited Six months ended 30 June 2004 RMB million	Pro forma Six months ended 30 June 2003 RMB million
Gross claims expenses	18,747	17,388
Less: Loss recovered from reinsurance	(3,106)	(3,312)
Net claims expenses	15,641	14,076
Add: Change in net loss and loss adjustment expense reserves	1,945	178
Add: Change in net provision for premium deficiency	—	(1)
Net claims incurred	17,586	14,253

## 6. OPERATING PROFIT

The Company's operating profit is arrived at after charging:

	Unaudited Six months ended 30 June 2004 RMB million	Pro forma Six months ended 30 June 2003 RMB million
Depreciation	706	854
Provision for doubtful accounts	78	11

## 7. TAX

	Unaudited Six months ended 30 June 2004 RMB million	Pro forma Six months ended 30 June 2003 RMB million
Current - PRC		
Charge for the period	456	44
Deferred	(129)	558
Total tax charge for the period	327	602

**8. DIVIDEND**

The Board of Directors does not recommend payment of an interim dividend in respect of the six months ended 30 June 2004 (six months ended 30 June 2003: Nil).

**9. EARNINGS PER SHARE**

The calculations of basic earnings per share for the six months ended 30 June 2004 and 2003 are based on:

	Unaudited Six months ended 30 June 2004 RMB million	Pro forma Six months ended 30 June 2003 RMB million
<b>Earnings</b>		
Net profit attributable to shareholders used in the basic earnings per share calculation	963	1,321
	Unaudited Six months ended 30 June 2004 million	Pro forma Six months ended 30 June 2003 million
<b>Shares</b>		
Number of ordinary shares used in the basic earnings per share calculation	11,142	8,000

The pro forma basic earnings per share for the six months ended 30 June 2003 has been computed by dividing net profit by 8,000 million shares, the number of shares issued and outstanding upon the formation of the Company on 7 July 2003, as if such shares have been outstanding throughout the period. The Company has no dilutive potential shares outstanding during the six months ended 30 June 2004.

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## 10. CASH AND CASH EQUIVALENTS AND TERM DEPOSITS

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Demand deposits	16,960	11,529
Cash in hand	58	32
Securities purchased under resale agreements with original maturity of less than 3 months	1,200	3,327
Deposits with banks and other financial institutions with original maturity of less than 3 months	2,156	3,116
Investments in securities with original maturity of less than 3 months	1,761	—
Cash and cash equivalents	22,135	18,004
Deposits with banks and other financial institutions with original maturity of more than 3 months	9,448	12,562
Total	31,583	30,566

## 11. TRADING SECURITIES

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Listed investments:		
Debt securities issued by the PRC central government	1,818	1,813
Debt securities issued by corporate entities	62	66
Mutual funds issued by banks and other financial institutions	3,213	3,690
	5,093	5,569
Unlisted investments:		
Debt securities issued by the PRC central government	228	525
Debt securities issued by banks and other financial institutions	740	—
	968	525
Total	6,061	6,094

Trading securities are investments in securities held for trading purposes and are stated at their fair value on the basis of their quoted market prices at 30 June 2004 and 31 December 2003, on an individual investment basis.

**11. TRADING SECURITIES** *(Continued)*

A maturity profile of the debt securities classified as trading securities according to their contractual maturity dates is as follows:

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Less than 3 months but not on demand	298	199
Less than 1 year but more than 3 months	670	326
Less than 5 years but more than 1 year	1,749	1,813
More than 5 years	131	66
	2,848	2,404

**12. NON-TRADING SECURITIES**

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Listed investments:		
Debt securities issued by the PRC		
central government	2,900	1,864
Debt securities issued by corporate entities	666	280
	3,566	2,144
Unlisted investments:		
Debt securities issued by the PRC		
central government	4,528	4,441
Debt securities issued by banks and		
other financial institutions	1,238	1,142
Debt securities issued by corporate entities	1,691	1,373
Mutual funds issued by banks and		
other financial institutions	4,103	1,665
	11,560	8,621
	15,126	10,765

At 30 June 2004 and 31 December 2003, non-trading securities are carried at fair value. The unlisted investments are traded on over-the-counter market in the PRC.

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## 12. NON-TRADING SECURITIES (Continued)

A maturity profile of the debt securities classified as non-trading securities according to their contractual maturity dates is as follows:

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Less than 1 year but more than 3 months	162	201
Less than 5 years but more than 1 year	4,626	3,696
More than 5 years	6,235	5,203
	11,023	9,100

## 13. HELD-TO-MATURITY SECURITIES

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Unlisted investments:		
Subordinated debt securities issued by banks and other financial institutions	1,100	—

A maturity profile of the debt securities classified as held-to-maturity securities according to their contractual maturity dates is as follows:

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Less than 5 years but more than 1 year	600	—
More than 5 years	500	—
	1,100	—

## 14. PREMIUMS RECEIVABLES AND AGENTS' BALANCES, NET

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Premiums receivables and agents' balances	4,251	2,095
Less: Allowance for doubtful accounts	(161)	(83)
	4,090	2,012

An ageing analysis of the premiums receivable and agents' balances at the balance sheet date, based on payment due date, and net of provisions, is as follows:

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Within 3 months	3,409	1,622
Over 3 months but less than 6 months	681	345
Over 6 months	—	45
	4,090	2,012

## 15. RECEIVABLES FROM REINSURERS

An ageing analysis of the receivables from reinsurers at the balance sheet date is as follows:

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Within 3 months	631	536
Over 3 months but less than 6 months	110	70
Over 6 months	137	50
	878	656

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**16. PREPAYMENTS AND OTHER RECEIVABLES**

Included in prepayments and other receivables was an amount due from certain provincial and municipal governments totaling RMB1,210 million (31 December 2003: RMB1,210 million). During 1999, pursuant to the instruction from the State Council as part of the restructuring of the PRC insurance industry, the Company acquired the commercial insurance business of certain provincial and municipal governments. On the date of the acquisition, the net liabilities assumed amounted to RMB1,210 million, which mainly consisted of unearned premium reserves and loss and loss adjustment expense reserves, net of cash and cash equivalents.

On 30 May 2003, the Ministry of Finance issued a notice to the provincial and municipal governments instructing them to settle the amount with the Company by 31 December 2003. As of 30 June 2004, the Company was in the process of negotiating with the relevant provincial and municipal governments to settle the amount. PICC Holding Company has undertaken to the Company that the amount will be fully recovered by the Company. Accordingly, no provision has been made against this amount at 30 June 2004 (31 December 2003: nil).

**17. PAYABLES TO REINSURERS**

Payables to reinsurers are analysed as follows:

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Reinsurance balances payable	912	1,132
Reinsurance funds withheld	801	846
	1,713	1,978

**18. ISSUED CAPITAL**

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
<b>Shares</b>		
Registered, issued and fully paid:		
7,685,820,000 domestic shares of RMB1.00 each	7,686	7,686
3,455,980,000 H shares of RMB1.00 each	3,456	3,456
	11,142	11,142

The Company does not have a share option scheme.

**19. SUBORDINATED LOAN**

On 10 October 2003, the Company signed a loan agreement with China Development Bank which advanced a subordinated loan of RMB2,000 million to the Company. The loan is unsecured, bears interest at 90% of the People's Bank Of China five-year borrowing interest rate per annum and is repayable in November 2023.

**20. CONTINGENT LIABILITIES**

Owing to the nature of insurance business, the Company is involved in legal proceedings in the ordinary course of business, including being the plaintiff or the defendant in litigation and arbitration. Such legal proceedings mostly involve claims on the Company's insurance policies. While the outcome of such contingencies, lawsuits or other proceedings cannot be determined at present, management believes that any resulting liabilities will not have a material adverse effect on the financial position or operating results of the Company.

**21. OPERATING LEASE COMMITMENTS**

The Company leases certain of its land and buildings and motor vehicles under operating lease arrangements. Leases for properties are negotiated for terms ranging from one to twenty years, and those for motor vehicles for terms ranging between one to three years.

At 30 June 2004, the Company had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Within one year	280	296
In the second to fifth years, inclusive	575	681
After five years	21	54
	876	1,031

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**22. CAPITAL COMMITMENTS**

In addition to the operating lease commitments detailed in note 21 above, the Company had the following capital commitments at the balance sheet date:

	Unaudited 30 June 2004 RMB million	Audited 31 December 2003 RMB million
Contracted, but not provided for	228	81
Authorised, but not contracted for	118	236
	346	317

**23. RELATED PARTY TRANSACTIONS**

The Company conducts businesses with enterprises directly or indirectly owned or controlled by the PRC government ("state-owned enterprises"). Furthermore, the PRC government itself represents a significant customer of the Company both directly through its numerous authorities and indirectly through its numerous affiliates and other organisations. The Company considers that the sale of insurance products to the PRC government authorities and affiliates and other state-owned enterprises are in the ordinary and normal course of business in the PRC and has not disclosed such transactions as related party transactions.

In addition to the transactions and balances detailed elsewhere in these interim financial statements, the Company and PICC Holding Company, PICC Asset Management Company Limited and American International Group, a strategic shareholder of the Company, entered into a number of agreements after the Company's incorporation in connection with the Reorganisation. These agreements impact the results of the operations of the Company beginning from the respective dates. The relevant transactions during the six months ended 30 June 2004 are summarised as follows:

	Unaudited Six months ended 30 June 2004 RMB million
Property rental expenses to PICC Holding Company	105
Property rental income from PICC Holding Company	5
Motor vehicle rental expenses to PICC Holding Company	11
Motor vehicle rental income from PICC Holding Company	2
Management fee to PICC Asset Management Company Limited	17
Services fee income from PICC Holding Company	2

**23. RELATED PARTY TRANSACTIONS (Continued)**

The above transactions took place after the incorporation of the Company. Accordingly, no comparative information is available. Details of the terms of principal agreements entered into relating to the above transactions are consistent with those disclosed in the Company's first set of financial statements for the period from 7 July 2003 (date of incorporation) to 31 December 2003.

The above transactions also constitute connected transactions under the Main Board Listing Rules. Such transactions are exempted from disclosure by press notices under a waiver obtained from HKSE.

**24. APPROVAL OF INTERIM FINANCIAL STATEMENTS**

The interim financial statements for the six months ended 30 June 2004 were approved and authorised for issue by the Board of Directors on 20 August 2004.



## INDEPENDENT REVIEW REPORT TO THE BOARD OF DIRECTORS OF PICC PROPERTY AND CASUALTY COMPANY LIMITED

*(a joint stock company incorporated in the People's Republic of China with limited liability)*

We have been instructed by the Company to review the interim financial statements set out on pages 2 to 21.

### Respective responsibilities of directors and auditors

The Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of interim financial statements to be in compliance with Statement of Standard Accounting Practice 25 "Interim financial reporting" issued by the Hong Kong Society of Accountants and the relevant provisions thereof. The interim financial statements are the responsibility of, and have been approved by, the directors. It is our responsibility to form an independent conclusion, based on our review, on the interim financial statements and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

### Review work performed

We conducted our review in accordance with Statement of Auditing Standards 700 "Engagements to review interim financial reports" issued by the Hong Kong Society of Accountants. A review consists principally of making enquiries of management and applying analytical procedures to the interim financial statements and based thereon, assessing whether the accounting policies and presentation have been consistently applied unless otherwise disclosed. A review excludes audit procedures such as tests of controls and verification of assets, liabilities and transactions. It is substantially less in scope than an audit and therefore provides a lower level of assurance than an audit. Accordingly we do not express an audit opinion on the interim financial statements.

### Review conclusion

On the basis of our review which does not constitute an audit, we are not aware of any material modifications that should be made to the interim financial statements for the six months ended 30 June 2004.

**Ernst & Young**

*Certified Public Accountants*

Hong Kong

20 August 2004

## OVERVIEW

The Company is a leading property and casualty insurance company in the PRC providing a broad range of property and casualty insurance products and accidental injury insurance products for customers. In the first half of 2004, the Company's market share in the property and casualty insurance market was 63.3%.

The following table sets forth the net premiums earned, underwriting profit, net profit and total assets of the Company for the periods indicated.

	Six months ended 30 June	
	2004	2003 <sup>2</sup>
	(RMB in million)	
Net premiums earned	24,206	19,930
Underwriting profit <sup>1</sup>	1,429	1,461
Net profit	963	1,321
Total assets	93,705	80,288

<sup>1</sup> Underwriting profit represents net premiums earned minus net claims incurred, and after amortisation of deferred acquisition costs, insurance protection expense and general and administrative expenses.

<sup>2</sup> The comparative figures for the six months ended 30 June 2003 and the value of total assets as of 30 June 2003 were extracted from the Accountant's Report as set out in the Company's prospectus.

## RESULTS OF OPERATIONS

In the first half of 2004, the Company's turnover increased rapidly, underwriting profit remained flat, and investment return decreased significantly.

The following table sets forth selected financial information shown as percentages of net premiums earned for the periods indicated.

	Six months ended 30 June	
	2004	2003
	(%)	
Net premiums earned	100.0	100.0
Net claims incurred	(72.7)	(71.5)
Amortisation of deferred acquisition costs	(6.7)	(5.2)
Insurance protection expense	(1.3)	(1.3)
General and administrative expenses	(13.4)	(14.7)
Underwriting profit	5.9	7.3
Interest and dividend income	2.1	1.5
Net gains/(losses) on trading and non-trading securities	(2.1)	1.2
Finance costs	(0.3)	(0.1)
Interest expense credited to policyholders' deposits	(0.3)	(0.3)
Profit before taxation	5.3	9.6
Tax	(1.3)	(3.0)
Net profit	4.0	6.6
Loss ratio	72.7%	71.5%
Expense ratio	21.4%	21.2%
Combined ratio	94.1%	92.7%

## OPERATING RESULTS BY SEGMENT

The following table sets forth the net premiums earned, net claims incurred and amortisation of deferred acquisition costs by segment, analysed as percentages, for the periods indicated.

	Six months ended 30 June	
	2004	2003
	(%)	
<b>Net premiums earned</b>		
Motor vehicle	67.7	65.4
Commercial property	13.4	17.3
Homeowners	1.6	3.0
Other	17.3	14.3
<b>Total</b>	<b>100.0</b>	<b>100.0</b>
<b>Net claims incurred</b>		
Motor vehicle	80.2	75.1
Commercial property	7.1	11.3
Homeowners	0.6	1.2
Other	12.1	12.4
<b>Total</b>	<b>100.0</b>	<b>100.0</b>
<b>Amortisation of deferred acquisition costs</b>		
Motor vehicle	81.7	87.0
Commercial property	8.2	5.8
Homeowners	2.9	7.5
Other	7.2	(0.3)
<b>Total</b>	<b>100.0</b>	<b>100.0</b>

## TURNOVER

Turnover of the Company reached RMB35,389 million in the first half of 2004, representing an increase of 15.5% compared to RMB30,651 million in the first half of 2003. The increase was primarily due to a RMB4,810 million increase in turnover of the motor vehicle segment.

## NET PREMIUMS EARNED

Net premiums earned of the Company reached RMB24,206 million in the first half of 2004, representing an increase of 21.5% compared to RMB19,930 million in the first half of 2003. The increase was primarily due to an increase in turnover and a decrease in premiums ceded, which was partially offset by an increase in the change in net unearned premium reserves. Premiums ceded decreased from RMB5,720 million, or 18.7% of turnover, in the first half of 2003 to RMB4,803 million, or 13.6% of turnover, in the first half of 2004. The decrease was primarily due to a reduction in the statutory reinsurance rate from 15% in 2003 to 10% in 2004 under the requirements set out in the WTO Accession Protocol signed by the PRC. The increase in net unearned premium reserves in the first half of 2004 compared to the first half of 2003 was primarily due to the increase in net premiums written, which was in turn due to the increase in turnover and the decrease in premiums ceded.

## INTEREST AND DIVIDEND INCOME

Interest and dividend income of the Company reached RMB519 million in the first half of 2004, representing an increase of 72.4% compared to RMB301 million in the first half of 2003. The increase was primarily due to an increase in interest income from trading and non-trading securities and interest income from bank deposits of RMB146 million and RMB74 million, respectively. The increase in interest income from trading and non-trading securities was primarily due to an increase of RMB5,059 million in investments in debt securities in the first half of 2004 compared to the first half of 2003 (please refer to Accountant's Report as set out in the Company's prospectus for the value of investment in debt securities at 30 June 2003). The increase in interest income from bank deposits was mainly due to an increase of RMB2,320 million in higher interest-bearing structured deposits included in deposits with banks and other financial institutions with original maturity of more than three months.

## NET GAINS/(LOSSES) ON TRADING AND NON-TRADING SECURITIES

The Company's net losses on trading and non-trading securities amounted to RMB514 million in the first half of 2004, decreased RMB744 million compared to a net gain of RMB230 million in the first half of 2003. This was primarily due to a decrease in unrealised gain on trading securities. The unrealised gains in respect of mutual funds and debt securities decreased RMB641 million and RMB107 million, respectively, as a result of the subdued PRC securities markets.

## NET CLAIMS INCURRED

The Company's net claims incurred amounted to RMB17,586 million in the first half of 2004, representing an increase of 23.4% compared to RMB14,253 million in the first half of 2003. Loss ratio increased to 72.7% in the first half of 2004 compared to 71.5% in the first half of 2003. The increase was primarily due to a 31.6% increase in net claims incurred in the motor vehicle segment to RMB14,096 million in the first half of 2004 compared to RMB10,708 million in the first half of 2003. The increase was partially offset by a decrease in net claims incurred in the commercial property, liability, cargo and homeowners segments in the first half of 2004. Loss and loss adjustment expense reserves as of 30 June 2004 increased by RMB1,945 million as compared to 31 December 2003, due partly to an increase of RMB963 million in the loss and loss adjustment expense reserves for claims that occurred prior to 31 December 2003, after comparing the latest actuarial results as of 30 June 2004 to the actuarial results as of 31 December 2003.

## AMORTISATION OF DEFERRED ACQUISITION COSTS

Amortisation of deferred acquisition costs amounted to RMB1,626 million in the first half of 2004, representing an increase of 58.0% compared to RMB1,029 million in the first half of 2003. The increase was primarily due to an increase of RMB555 million in commission expenses to insurance intermediaries and agents and a decrease of RMB338 million in reinsurance commission in the first half of 2004 compared to the first half of 2003. The increase in commission expenses was primarily due to the increase in turnover and the decrease in reinsurance commission was primarily due to the decrease in premiums ceded.

## INSURANCE PROTECTION EXPENSE

According to the relevant PRC insurance law and regulations, the Company is required to accrue an insurance protection fund based on 1% of its retained premiums. Insurance protection expense of the Company amounted to RMB325 million in the first half of 2004, representing an increase of 26.0% compared to RMB258 million in the first half of 2003. The increase was primarily due to an increase in retained premiums.

## INTEREST EXPENSE CREDITED TO POLICYHOLDERS' DEPOSITS

Interest expense of the Company credited to policyholders' deposits was RMB78 million in the first half of 2004, representing an increase of 34.5% compared to RMB58 million in the first half of 2003. The increase was primarily due to an increase in deposits obtained from Golden Bull homeowners insurance products. Policyholders' deposits amounted to RMB9,154 million as of 30 June 2004, representing an increase of RMB1,133 million compared to RMB8,021 million as of 30 June 2003.

## FINANCE COSTS

Finance costs amounted to RMB66 million in the first half of 2004, representing an increase of RMB55 million compared to RMB11 million in the first half of 2003. The increase was primarily due to a RMB2,000 million subordinated loan issued by the Company in the second half of 2003, resulting in an increase in interest expense of RMB50 million.

## GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses of the Company amounted to RMB3,240 million in the first half of 2004, representing an increase of 10.6% compared to RMB2,929 million in the first half of 2003. The increase was primarily due to an increase of RMB171 million in personnel expenses, an increase of RMB52 million in operating lease charges and an increase of RMB67 million in provision for doubtful accounts.

## PROFIT BEFORE TAX

Profit before tax amounted to RMB1,290 million in the first half of 2004, representing a decrease of 32.9% compared to RMB1,923 million in the first half of 2003. The decrease was primarily due to a RMB744 million decrease in net gain on trading and non-trading securities, which was partially offset by an increase of 72.4% in interest and dividend income to RMB519 million in the first half of 2004 compared to RMB301 million in the first half of 2003.

## TAX

Tax was RMB327 million in the first half of 2004, representing a decrease of RMB275 million compared to RMB602 million in the first half of 2003. The Company's effective tax rate was 25.3% in the first half of 2004 compared to 31.3% in the first half of 2003, primarily due to an increase in non-taxable interest income from government bonds in the first half of 2004.

## NET PROFIT

Overall, the Company's net profit decreased 27.1% to RMB963 million in the first half of 2004 compared to RMB1,321 million in the first half of 2003. Basic earnings per share in the first half of 2004 was RMB0.086.

## COMBINED RATIO

The Company's combined ratio increased from 92.7% in the first half of 2003 to 94.1% in the first half of 2004, primarily due to an increase in loss ratio from 71.5% in the first half of 2003 to 72.7% in the first half of 2004 and an increase in expense ratio from 21.2% in the first half of 2003 to 21.4% in the first half of 2004.

## RESULTS OF SEGMENT OPERATIONS

### Motor Vehicle Insurance

	Six months ended 30 June	
	2004	2003
	(RMB in million)	
Turnover	24,197	19,387
Net premiums earned	16,377	13,028
Net claims incurred	(14,096)	(10,708)
Amortisation of deferred acquisition costs	(1,328)	(895)
Insurance protection expense	(231)	(168)
Segment profit before unallocated income and expenses	722	1,257
Loss ratio	86.1%	82.2%
Segment expense ratio	9.5%	8.2%
Segment combined ratio	95.6%	90.4%

Turnover of the motor vehicle segment increased 24.8% to RMB24,197 million in the first half of 2004 compared to RMB19,387 million in the first half of 2003. This increase was primarily due to an increase in the number of motor vehicles insured and the increase in premium rates. The Company insured 11.79 million motor vehicles in the first half of 2004, representing an increase of 2.42 million compared to the first half of 2003.

Net premiums earned of the motor vehicle segment amounted to RMB16,377 million in the first half of 2004, representing a 25.7% increase compared to RMB13,028 million in the first half of 2003. The increase was primarily due to the increase in turnover and the decrease in reinsurance premiums ceded. However, this was partially offset by the corresponding increase in the change in net unearned premium reserves.

Net claims incurred of the motor vehicle segment increased 31.6% to RMB14,096 million in the first half of 2004 from RMB10,708 million in the first half of 2003. Loss ratio increased to 86.1% in the first half of 2004 compared to 82.2% in the first half of 2003. The increase in net claims incurred was due to a number of factors including the continuing effect of the deregulation in the terms and premium rates of motor vehicle insurance, changes in laws governing road traffic control and compensation for personal injury, increasing number of private motor vehicles, increasing number of new drivers and the failure to improve road conditions to accommodate increasing traffic volume, as well as the substantial increase in small claims leading to an increase in claims settlement expenses. The number of claims for motor vehicle insurance increased substantially in the first half of 2004. However, the effect of such increase on net claims incurred was partially offset by the decrease in average payment per claim. Loss and loss adjustment expense reserves of the motor vehicle segment as of 30 June 2004 increased RMB1,477 million compared to 31 December 2003, primarily due to the deregulation of terms and premium rates of the motor vehicle insurance, which came into effect in the PRC in January 2003. The Company increased the loss and loss adjustment expense reserves for motor vehicle insurance claims that occurred prior to 31 December 2003 by RMB1,178 million, after comparing the latest actuarial results as of 30 June 2004 to the actuarial results as of 31 December 2003.

Amortisation of deferred acquisition costs charged to the motor vehicle segment increased 48.4% to RMB1,328 million in the first half of 2004 compared to RMB895 million in the first half of 2003. The increase was primarily due to the increase in turnover causing a corresponding increase in commission expenses, and the decrease in reinsurance commission.

Insurance protection expense charged to the motor vehicle segment increased 37.5% to RMB231 million in the first half of 2004 compared to RMB168 million in the first half of 2003 due to an increase in retained premiums.

Due to an increase in amortisation of deferred acquisition costs and an increase in insurance protection expense, the expense ratio of the motor vehicle segment increased to 9.5% in the first half of 2004 compared to 8.2% in the first half of 2003.

Overall, the motor vehicle segment recorded a RMB722 million profit before unallocated income and expenses in the first half of 2004, representing a decrease of 42.6% compared to RMB1,257 million in the first half of 2003.

## Commercial Property Insurance

	Six months ended 30 June	
	2004	2003
	(RMB in million)	
Turnover	5,145	5,221
Net premiums earned	3,238	3,441
Net claims incurred	(1,248)	(1,605)
Amortisation of deferred acquisition costs	(133)	(60)
Insurance protection expense	(45)	(42)
Segment profit before unallocated income and expenses	1,812	1,734
Loss ratio	38.5%	46.6%
Segment expense ratio	5.5%	3.0%
Segment combined ratio	44.0%	49.6%

Turnover of the commercial property segment decreased 1.5% to RMB5,145 million in the first half of 2004 compared to RMB5,221 million in the first half of 2003, primarily due to a decrease in average premium rates resulting from intense market competition, and also due to reduction of exposure to certain high risk customers with an objective to improve underwriting quality.

Net premiums earned of the commercial property segment reached RMB3,238 million in the first half of 2004, representing a 5.9% decrease compared to RMB3,441 million in the first half of 2003. The decrease was primarily due to a decrease in the turnover and an increase in the change in net unearned premium reserves.

Net claims incurred of the commercial property segment decreased 22.2% to RMB1,248 million in the first half of 2004 compared to RMB1,605 million in the first half of 2003. The Company has introduced stringent measures on underwriting criteria in relation to commercial property segment to monitor risk exposure and reduce underwriting risks. These measures led to an improvement in the results of the Company's commercial property segment and a reduction in claims. In addition, the Company also successfully reduced net claims incurred by adding limitations to the scope of liabilities and by reducing exposure to catastrophe losses. The decrease in net claims incurred was larger than the decrease in net premiums earned, resulting in an improvement in loss ratio for the commercial property segment from 46.6% in the first half of 2003 to 38.5% in the first half of 2004.

Amortisation of deferred acquisition costs charged to the commercial property segment increased 121.7% to RMB133 million in the first half of 2004 compared to RMB60 million in the first half of 2003. It was primarily because the premium income of the commercial property segment was recognised in a faster manner in the first half of 2004 when compared to the first half of 2003, causing a decrease in the ratio of unearned premium reserves to gross premiums written. The amount of acquisition costs to be deferred decreased accordingly.

Insurance protection expense charged to the commercial property segment increased 7.1% to RMB45 million in the first half of 2004 compared to RMB42 million in the first half of 2003, primarily due to an increase in retained premiums.

Due to an increase in amortisation of deferred acquisition costs and an increase in insurance protection expense, the segment expense ratio of the commercial property segment increased to 5.5% in the first half of 2004 compared to 3.0% in the first half of 2003.

Overall, the commercial property segment recorded a RMB1,812 million profit before unallocated income and expenses in the first half of 2004, representing an increase of 4.5% compared to RMB1,734 million in the first half of 2003.

#### Homeowners Insurance

	Six months ended 30 June	
	2004	2003
	(RMB in million)	
Turnover	793	736
Net premiums earned	378	604
Net claims incurred	(103)	(178)
Amortisation of deferred acquisition costs	(47)	(77)
Interest and dividend income	53	99
Net gains/(losses) on trading and non-trading securities	(7)	58
Interest expense credited to policyholders' deposits	(78)	(58)
Insurance protection expense	(8)	(7)
Segment profit before unallocated income and expenses	188	441
Loss ratio	27.3%	29.5%
Segment expense ratio	14.6%	13.9%
Segment combined ratio	41.9%	43.4%

Turnover of the homeowners segment increased 7.7% to RMB793 million in the first half of 2004 compared to RMB736 million in the first half of 2003. The increase was primarily due to the increased effort in expanding the homeowners insurance market.

Net premiums earned of the homeowners segment decreased 37.4% to RMB378 million in the first half of 2004 compared to RMB604 million in the first half of 2003. The decrease was primarily due to an increase in the number of policies with longer insurance periods. The percentage of premium income in respect of policies incepting with longer insurance periods increased from 23.8% in the first half of 2003 to 55.9% in the first half of 2004, resulting in a significant increase in unearned premium reserves.

Net claims incurred of the homeowners segment decreased 42.1% to RMB103 million in the first half of 2004 compared to RMB178 million in the first half of 2003. Loss ratio decreased to 27.3% in the first half of 2004 compared to 29.5% in the first half of 2003, primarily due to a decrease in net claims incurred.

Amortisation of deferred acquisition costs charged to the homeowners segment decreased 39.0% to RMB47 million in the first half of 2004 compared to RMB77 million in the first half of 2003. The decrease was primarily due to an increase in the premium income with longer insurance periods, causing an increase in the ratio of unearned premium reserves to gross premiums written.

Insurance protection expense charged to the homeowners insurance segment increased to RMB8 million in the first half of 2004 compared to RMB7 million in the first half of 2003, primarily due to an increase in retained premiums.

The segment expense ratio of the homeowners segment increased to 14.6% in the first half of 2004 compared to 13.9% in the first half of 2003.

The interest and dividend income deriving from policyholders' deposits of the homeowners segment decreased RMB46 million to RMB53 million in the first half of 2004 compared to RMB99 million in the first half of 2003, mainly because the increase in interest and dividend income deriving from the deposits obtained from Golden Bull homeowners insurance products was less than the increase in fixed rate interest paid to the policyholders.

Interest expense credited to policyholders' deposits of the homeowners segment increased 34.5% to RMB78 million in the first half of 2004 from RMB58 million in the first half of 2003, mainly due to an increase in deposits obtained from Golden Bull homeowners insurance products.

Overall, the homeowners segment recorded a RMB188 million profit before unallocated income and expenses in the first half of 2004, representing a decrease of 57.4% compared to RMB441 million in the first half of 2003.

## Other Insurance Segments

The Company's other insurance segments include cargo, liability, accidental injury, aviation, construction, marine hull and oil and gas, etc.

	Six months ended 30 June	
	2004	2003
	(RMB in million)	
<b>Turnover</b>		
Cargo	1,527	1,555
Liability	1,094	1,412
Accidental injury	836	849
Other	1,797	1,491
<b>Total</b>	<b>5,254</b>	<b>5,307</b>
<b>Net premiums earned</b>		
Cargo	1,710	1,177
Liability	942	1,112
Accidental injury	851	37
Other	710	531
<b>Total</b>	<b>4,213</b>	<b>2,857</b>
Net claims incurred	(2,139)	(1,762)
Amortisation of deferred acquisition costs	(118)	3
Insurance protection expense	(41)	(41)
Segment profit before unallocated income and expenses	1,915	1,057
Loss ratio	50.8%	61.7%
Segment expense ratio	3.8%	1.3%
Segment combined ratio	54.6%	63.0%

Turnover of the other insurance segments decreased 1.0% to RMB5,254 million in the first half of 2004 compared to RMB5,307 million in the first half of 2003. The decrease was primarily due to a fall in turnover of the liability segment by 22.5% in the first half of 2004 compared to the first half of 2003, which was primarily due to the promulgation and implementation of the "Regulations on Industrial Accident Insurance" in the first half of 2004, largely impacting employers' commercial liabilities and the operating results of the liability segment.

Net premiums earned of the other insurance segments increased 47.5% to RMB4,213 million in the first half of 2004 compared to RMB2,857 million in the first half of 2003. This increase was primarily due to a decrease in change in net unearned premium reserves, causing an increase of RMB814 million in net premiums earned of the accidental injury insurance segment and an increase of RMB533 million in net premiums earned of the cargo segment; and also due to a decrease of RMB86 million in premiums ceded.

Net claims incurred of the other insurance segments increased 21.4% to RMB2,139 million in the first half of 2004 compared to RMB1,762 million in the first half of 2003. The increase in net claims incurred was primarily due to an increase of RMB522 million in net claims incurred of the accidental injury segment. Net claims incurred of the accidental injury segment increased mainly because the Company entered into the accidental injury insurance market in the first half of 2003, whilst the turnover was comparatively low and the number of claims was small. By introducing stringent measures on underwriting criteria and improving claims management, the loss ratio of the other insurance segments decreased to 50.8% in the first half of 2004 compared to 61.7% in the first half of 2003.

Amortisation of deferred acquisition costs charged to other insurance products amounted to RMB118 million in the first half of 2004. There was a write-back of RMB3 million in the first half of 2003 due to reinsurance commission.

Insurance protection expense charged to the other insurance segments was RMB41 million in the first half of 2004, the same as that in the first half of 2003.

Overall, the other insurance segments recorded a RMB1,915 million profit before unallocated income and expenses, representing an increase of 81.2% compared to RMB1,057 million in the first half of 2003.

## GEARING RATIO

As of 30 June 2004, the gearing ratio<sup>3</sup> of the Company was 79.4%, representing an increase of 1.6 percentage points compared to 77.8% as of 31 December 2003.

## DEVELOPMENT OF NEW PRODUCTS

In the first half of 2004, the Company developed 94 new insurance coverages in, amongst others, liability insurance, accidental injury insurance, motor vehicle insurance and commercial property insurance product lines, of which 26 are stand-alone coverages and 68 are supplementary coverages.

In the second half of 2004, the Company will strengthen its market research, focus on targeted customer groups and specific channels, and design customised products. The Company will also actively strengthen its cooperation with American International Group, Inc. ("AIG"), improve the product design of accidental injury and short-term health insurance and focus on the pilot launch of such products.

## CASH FLOW

	Six months ended 30 June	
	2004	2003
	(RMB in million)	
Net cash inflow from operating activities	8,102	7,286
Net cash outflow from investing activities	(3,132)	(2,182)
Net cash inflow/(outflow) from financing activities	(839)	1,064
Net increase in cash and cash equivalents	4,131	6,168

<sup>3</sup> Gearing ratio is defined as total liabilities (excluding subordinated loan) divided by total assets.

Net cash generated from operating activities in the first half of 2004 was RMB8,102 million, representing an increase of 11.2% compared to the first half of 2003. The increase was primarily due to an increase in premiums received in cash in the first half of 2004, which was partially offset by an increase in claims payment in cash.

Net cash used by the Company in investing activities in the first half of 2004 was RMB3,132 million, representing an increase of RMB950 million compared to the first half of 2003. Such increase was primarily due to an increase in funds used for purchasing trading and non-trading securities and held-to-maturity securities.

Net cash used by the Company in financing activities in the first half of 2004 was RMB839 million. Net cash generated from financing activities in the first half of 2003 was RMB1,064 million. The increase in net cash used in financing activities was primarily due to the payment of RMB644 million special dividend to the Company's ultimate holding company, PICC Holding Company, in the first half of 2004.

Net increase in cash and cash equivalents of the Company in the first half of 2004 was RMB4,131 million, representing a decrease of 33.0% compared to the first half of 2003.

## LIQUIDITY

The Company's cash flow is primarily derived from the cash generated from operating activities, mainly cash from insurance premiums received. Additional liquidity sources include interest and dividend income, proceeds from matured investments, disposal of assets and financing activities. The Company's liquidity needs consist principally of payment of claims and other obligations under outstanding insurance policies, capital expenditure, operating expenses, tax payments, dividend payments and investment needs.

The Company has entered into a subordinated loan agreement with China Development Bank on 10 October 2003 in respect of RMB2,000 million. This loan is unsecured and bears interest at a rate which is equal to 90% of the 5-year lending rate fixed by the People's Bank of China. The loan comes due in November 2023.

The Company obtained a 10-year revolving credit facility from China Development Bank for up to RMB10 billion on 26 August 2003. Each drawdown made under that facility is repayable within one year. As of the date of this interim report, no amount has been drawn down under that facility.

Save for the subordinated loan and the credit facility mentioned above, the Company does not obtain working capital by borrowing.

The Company expects that it can fund its working capital needs in the future from cash generated from operating activities. The Board of Directors is of the opinion that the Company has sufficient working capital.

## CAPITAL EXPENDITURE

The capital expenditure of the Company has primarily been for property construction, acquisition of motor vehicles and development of information systems. Capital expenditure was RMB103 million in the first half of 2004.

Save for the plan for a new headquarters building mentioned in the Company's 2003 Annual Report, there were no other material capital expenditure in the first half of 2004. The Company believes that it has sufficient capital resources to fully satisfy its capital expenditure plan and its working capital requirements.

## CONTINGENT LIABILITIES

Owing to the nature of the insurance business, the Company is involved in legal proceedings in the ordinary course of business, as plaintiff or defendant. Such legal proceedings mostly involve claims on the Company's insurance policies. While the outcomes of such contingencies or legal proceedings cannot be determined at present, the Company believes that any resulting liabilities will not have a material adverse effect on the financial position or operating results of the Company.

## INTEREST RATE RISK

The Company's holding in fixed income investments is subject to interest rate risk. The Company also invests in floating rate instruments, interest proceeds from which can rise and fall due to changes in interest rates. The Company's holding in mutual funds is also exposed to price fluctuations caused by changes in interest rates. The Company manages exposure to risks associated with interest rate fluctuations through active review of the investment portfolio and consultation with financial investment experts. The goal is to maintain liquidity and to generate stable returns.

## CREDIT RISK

The Company is subject to credit risk on investments such as corporate bonds and mutual funds. The Company diligently manages credit risk by analysing the creditworthiness of companies prior to making investments as well as strictly following the CIRC guidelines which only permit investments in corporate bonds with rating higher than AA. The Company is also subject to credit risk with respect to amounts owed to it by reinsurers. As a result, except when dealing with national reinsurers such as China Property and Casualty Reinsurance Company Ltd., the Company only purchases reinsurance from reinsurers with A.M. Best ratings of at least A-, and pays particular attention to their creditworthiness and financial condition.

## EXCHANGE RATE RISK

The Company conducts its business primarily in Renminbi, which is also its functional and financial reporting currency. However, a portion of its business (including underwriting certain international cargo insurance and aviation insurance) are conducted in foreign currencies, typically US dollars. A portion of its claims and liabilities is also denominated in foreign currencies, typically US dollars.

Most of the Company's sales are domestic and as such it has a limited amount of foreign currency denominated accounts receivable. Foreign exchange transactions under the Company's capital account are subject to foreign exchange regulations and require the approval of the State Administration of Foreign Exchange. Foreign exchange policies adopted by the PRC government could cause future exchange rates to vary.

## HEDGING INSTRUMENTS

The use of funds in Renminbi and foreign currencies by insurance companies in the PRC is subject to the regulatory control by regulatory bodies of the PRC. Therefore, the Company does not use any financial instruments for hedging purposes.

## LOOKING FORWARD

The Company anticipates its results of operations to improve in the second half of 2004 over the same period last year. In order to maximise value for shareholders, the Company will focus on refining the “three centers” (the underwriting center, claims center, and finance center), accelerating settlement of claims while maintaining quality of underwriting and claims, improving the application of information technology, strengthening actuarial ability, adjusting its business structure to focus more on profitable non-motor vehicle insurance business. The Company will also enhance its cooperation with AIG and refine the pilot launch of the accidental injury and short-term health insurance products. The Company will further enhance its risk control in its use of funds to improve investment profitability.

## EMPLOYEES

As of 30 June 2004, the Company had 62,962 employees. In the first half of 2004, the Company's personnel expenses totalled RMB1,832 million. The Company makes contributions to retirement plans and social medical insurance plans for its employees. The Company enhances the performance and efficiency of employees through providing various career development paths, enhancing employees training and implementing performance review to its employees. The Company believes its relationship with its employees to be good.

## SHARE APPRECIATION RIGHTS PLAN

At the shareholders' meeting of the Company held on 30 July 2003, the Senior Management Share Appreciation Rights Plan (the "Share Appreciation Rights Plan"), which was designed to align the financial interests of senior management with the Company's results of operations and the performance of its H shares, was approved. No shares will be issued under the plan. Therefore, the shareholdings of shareholders will not be diluted. In the first half of 2004, no share appreciation right was granted under the Share Appreciation Rights Plan.

On 22 July 2004, the Company granted share appreciation rights to 76 senior management personnel, representing 28,628,000 shares, equivalent to 0.83% of the Company's total issued H shares, under the Share Appreciation Rights Plan.

## DIRECTORS', SUPERVISORS' AND CHIEF EXECUTIVE'S INTEREST IN SHARES

The following sets forth the interests or short positions in the shares, underlying shares or debentures of the Company or any of its associated corporations (as defined in the Securities and Futures Ordinance (the "SFO")) held by the directors, supervisors and chief executive of the Company as at 30 June 2004, which was recorded in the register required to be kept under section 352 of the SFO and which was required to be notified to the Company and HKSE under the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as contained in Appendix 10 to the Main Board Listing Rules.

Director	Capacity in which the shares are held	Number of shares held
Mr. Cheng Wai Chee, Christopher	Controlled Corporation ( <i>Note</i> )	50,000 H Shares

*Note: Such shares were directly held by Wing Tai Corporation Limited and were indirectly held by Wing Tai (Cheng) Holdings Limited and Renowned Development Limited. Mr. Cheng controls more than one-third of the votes at the shareholders' general meeting of the above companies. The interests disclosed above are long positions in the shares of the Company.*

Save as disclosed above, none of the other directors, supervisors or chief executive of the Company had any interest or short position in any shares, underlying shares or debentures of the Company or any of its associated corporations as at 30 June 2004 as recorded in the register required to be kept under section 352 of the SFO, or as notified pursuant to the Model Code.

## CHANGE OF DIRECTORS AND SUPERVISORS

The following sets forth the changes of directors and supervisors from 1 January 2004 to the date of this interim report:

Mr. Lu Zhengfei was appointed as an Independent Non-executive Director of the Company on 24 February 2004.

Mr. Tse Sze-Wing, Edmund was appointed as a Non-executive Director of the Company on 15 June 2004.

Mr. Qiao Lin, a Non-executive Director of the Company, has submitted an application for resignation to the Board of Directors on 20 August 2004 because he has retired. The Board of Directors has accepted his resignation on the same day.

As at the date of this interim report, the directors of the Company are Mr. Tang Yunxiang (Chairman of the Board), Mr. Wang Yi (Vice Chairman of the Board, Executive Director), Mr. Wang Yincheng (Executive Director), Ms. Liu Zhenghuan (Executive Director), Mr. Fu Zhu (Executive Director, Secretary of the Board), Mr. Ding Yunzhou (Non-executive Director), Mr. Zhou Shurui (Non-executive Director), Mr. Tse Sze-Wing, Edmund (Non-executive Director), Mr. Cheng Wai Chee, Christopher (Independent Non-executive Director), Mr. Wong Tung Shun, Peter (Independent Non-executive Director) and Mr. Lu Zhengfei (Independent Non-executive Director).

As at the date of this interim report, the supervisors of the Company are Mr. Deng Zhaoyu (Chairman of Supervisory Committee), Mr. Tang Wei (Supervisor) and Mr. Liu Qilong (Supervisor).

## MODEL CODE

All directors of the Company have confirmed, at the enquiry of the Company, that they had complied with the required standard as set out in the Model Code during the six months ended 30 June 2004.

## SUBSTANTIAL SHAREHOLDERS

As at 30 June 2004, the following shareholders were shown to have an interest of 5% or more in the issued share capital of the Company as recorded in the register required to be kept under section 336 of the SFO:

Types of shares	Shareholder	Number of Shares held		Percentage of Issued Share Capital
		Directly held	Indirectly held	
Domestic Shares	PICC Holding Company	7,685,820,000		69.0%
H Shares	AIG (Note 1)		1,103,038,000	9.9%
H Shares	Birmingham Fire Insurance Company of Pennsylvania ("BFIC") (Note 1)	562,549,380		5.05%

Notes: 1. AIG is the ultimate controlling company of BFIC, hence BFIC's interests are deemed to be AIG's interests.  
2. The interests disclosed above are long positions in the shares of the Company.

Save as disclosed above, so far as the Board of Directors is aware, as at 30 June 2004, no other person had any interests or short positions in the shares or underlying shares of the Company required to be recorded in the register required to be kept pursuant to section 336 of the SFO.

## REPURCHASE, SALE OR REDEMPTION OF THE COMPANY'S SECURITIES

The Company did not purchase, sell or redeem any of its listed securities in the first half of 2004.

## CODE OF BEST PRACTICE

So far as the Board of Directors is aware, apart from the passing away of Mr. Yan Dawu, who was an Independent Non-executive Director of the Company and the chairman of the audit committee of the Board of Directors (the "Audit Committee"), that resulted in the Audit Committee failing to fulfil the requirement of having a majority of Independent Non-executive Directors under the Code of Best Practice as set out in Appendix 14 to the Main Board Listing Rules during the period from 1 January 2004 to 24 February 2004, the Company had complied with the Code of Best Practice in the first half of 2004. The Company had appointed Mr. Lu Zhengfei, an Independent Non-executive Director, as the chairman of the Audit Committee on 24 February 2004, to fill the vacancy of Mr. Yan Dawu.

## AUDIT COMMITTEE

The Company has established the Audit Committee in September 2003 to review and supervise the financial reporting process and internal control of the Company. The Audit Committee has reviewed the Company's interim financial statements for the six months ended 30 June 2004.

Members of the Audit Committee from 24 February 2004 to 30 June 2004 are as follows:

Chairman: Mr. Lu Zhengfei

Members: Mr. Cheng Wai Chee, Christopher and Mr. Ding Yunzhou

## AUDITORS

At the annual general meeting held on 15 June 2004, resolution was passed to re-appoint Ernst & Young as the auditors of the Company for the year 2004, with a term of office until the next annual general meeting of the Company.

By Order of the Board  
Tang Yunxiang  
*Chairman*

Beijing, PRC  
20 August 2004